Managing risk, enabling trade

November 2018

market monitor

Focus on steel and metals performance and outlook

In this issue...

On the following pages we indicate the general outlook for each sector featured using these symbols:

Excellent
The credit risk situation in the sector is strong / business performance in the sector is strong compared to its long-term trend

Good
The credit risk situation in the sector is benign / business performance in the sector is above its long-term trend

Fair
The credit risk situation in the sector is average / business performance in the sector is stable

Poor
The credit risk in the sector is relatively high / business performance in the sector is below its long-term trend

Bleak
The credit risk in the sector is poor / business performance in the sector is weak compared to its long-term trend

More turbulent waters ahead?

In 2017 and H1 of 2018 the steel and metals industry has continued its rebound in most markets. However, the World Steel Association (WSA) forecasts that worldwide apparent steel use will increase just 0.7% in 2019 after growing 1.8% in 2018 and 4.7% in 2017.

While the direct impact of US steel and aluminium import tariffs has, so far, remained limited for most countries covered by this Market Monitor issue, uncertainties in the market have increased. For instance, the EU initiated safeguarding and anti-dumping measures in order to avert low prices and cheap imports. Due to the US tariffs, some steel producers like China, Russia, Turkey and South Korea have begun to redirect their exports. The outcome of the mounting trade disputes will influence the price development in 2019.

The steel rebound is mainly driven by cyclical factors, while fundamental structural issues remain. Overcapacity remains a major issue, and the global capacity utilisation rate remains low compared to the pre-2008 credit crisis years. Steel remains very susceptible to political and economic risk factors, such as additional protectionism (especially the escalation of the Sino-US trade conflict), China's hard landing, Brexit, an economic downturn in the EU and capital outflows from emerging markets. Should any of these risks materialise, it could immediately lead to a serious downturn in regional or global steel demand.

France

- Overcapacity remains an issue
- The insolvency level is expected to remain low
- Non-payments have increased

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector			✔		
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

In 2017 and H1 of 2018 the French steel and metals sector benefited from higher sales prices, coupled with dynamic demand from construction and automotive as well as a rebound of agricultural machinery. Revenues increased by 2%-3% on average, and operating margins of businesses have improved. That said, steel and metal businesses dependent on the oil and gas industry (mainly in the special steel manufacturing segment) continued to suffer from subdued demand.

The French steel and metal sector is just marginally impacted by US import tariffs (the US market accounts for only 4% of French steel and metals exports). However, in H2 of 2018 the situation for steel and metal businesses has started to deteriorate, due to lower demand from the construction sector, a generally decreasing business climate, increasing competition leading to lower margins, and the fear of price decreases triggered by excessive global supply.

Overcapacity remains an issue in French steel trading activity, despite falling to 15% from 25% a couple years ago following continued business consolidations and rationalisations. Operating margins generally remain low for many small players, especially smaller steel/metal traders, wholesalers and processors. Some smaller businesses, however, are able to operate in niche segments that provide higher margins.

Steel businesses are generally highly dependent on bank finance, due to high capital expenditures when operating upstream, and/or the need for short-term facilities to finance working capital requirements and inventories. Currently the willingness of banks to provide credit to the sector can be described as neutral.

The insolvency level is expected to remain low in 2018 and 2019, mainly because many steel and metals traders and wholesalers are able to adapt with a flexible cost structure. That is unless they

France: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	2.3	1.6	1.7
Sector value added growth (%)	-1.2	0.9	1.6

Average sector growth over the past 3 years (%)	-4.1
Average sector growth over the past 5 years (%)	-1.3
Degree of export orientation	medium
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

have a high level of inventories to finance. However, payment delays or rescheduling schemes are currently on an upward trend, as producers are facing cash pressure due to heavier working capital requirements while not always having adequate liquidity at hand.

French steel/metals sector

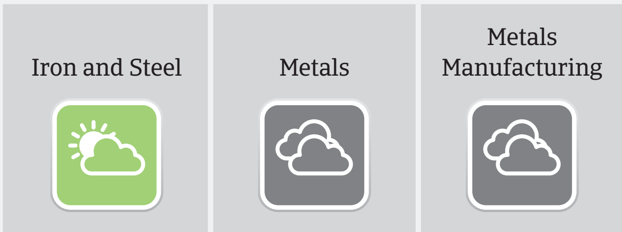
Strengths	Less overcapacity than in the past due to concentration and rationalisation
	The rebound since 2016 has helped to make businesses more resilient
Weaknesses	High financial needs
	Low margins due to stiff competition
	Financing new investments is an issue for many businesses

Source: Atradius

Our underwriting stance is generally open for the iron and steel and the metal recycling segments. The latter has experienced a strong rebound in 2017 and 2018 after two difficult years, with higher sales and improved margins. As many businesses in the general metals segment suffer from fierce competition and higher working capital requirement, our underwriting stance is neutral. The same accounts for metals manufacturing, where capacity problems, cash flow pressure and difficulties absorbing new investments are issues. Our underwriting is more restrictive for the steel foundry segment, which is facing difficulties due to overcapacities, a heavy cost structure and high production costs.

In the steel and metals industry, where both overcapacity and volatile prices are a concern, conditions can change quickly, especially if decreasing revenues and margins are not bolstered (in time) by cost management. Prudent inventory management has become a key factor for cost optimisation and absorbing sudden price decreases.

Performance forecast along subsectors



Source: Atradius

Germany

- More challenges ahead in the medium-term
- Increased production in 2017 and H1 of 2018
- Payments take between 30 and 45 days on average

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance			✔		
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months		✔			
General demand situation (sales)		✔			

Source: Atradius

According to the World Steel Association, German steel production increased 3.5% year-on-year in 2017, to 43.6 million tons. Steel production grew again between January and August 2018, by 3% year-on-year. German steel demand is expected to grow only slightly in 2018, by 0.5%, and to level off in 2019.

German steel producers have benefitted from price increases in 2017 and H1 of 2018, leading to better results and improved margins. The general economic upturn and an investment rebound in the oil and gas sector have led to an improved order situation, especially for the pipes and tubes segment.

The general equity and liquidity of steel businesses in Germany are better than the manufacturing industry average, except for small wholesalers without pre-fabrication and/or steel service activities. Banks are generally willing to provide loans to the steel and metals sector.

So far, the immediate impact of US import tariffs on steel and aluminium is considered to be low (the US accounts for just 1.5 % of German steel/aluminium exports). However, the risk of declining steel prices as a result of additional steel inflow into the EU remains, despite the current safeguarding measures. It is expected that both prices and margins will remain stable at best. Another downside risk is a sharp deceleration of EU economic growth.

Besides issues like punitive tariffs and trade barriers there are persistent structural challenges, such as volatile commodity and sales prices and overcapacities, while the number of overseas competitors from Africa, Asia and South America climbing up the value chain has increased, putting additional pressure on prices and margins. At the same time, the EU emission trading scheme and high energy costs in Germany threaten to increase the financial burden for German steel and metals businesses. Transport costs are sharply increasing due to a current truck driver shortage, and the situation is expected to worsen in the coming years.

Germany: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	2.2	1.8	1.6
Sector value added growth (%)	3.6	-1.7	3.9

Average sector growth over the past 3 years (%)	1.0
Average sector growth over the past 5 years (%)	1.7
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

In the medium- and long-term, decreasing demand for steel and metals from the automotive sector, as a key buyer industry (due to a shift to electric engines and lighter car bodies), could severely affect the sector.

We have seen no changes in the payment behaviour of companies in the steel and metals sector over the past couple of months, with payments taking, on average, between 30 and 45 days. The level of German steel and metal business failures has remained low, and no major change is expected in 2018 or 2019.

Our underwriting stance is mainly positive or neutral for German steel and metal businesses. While we are generally open for the iron and steel producer segment, we are neutral on metals, as smaller and medium-sized wholesalers in this segment often show low equity and tight margins. The same accounts for metal manufacturing, especially businesses that supply the automotive industry. In this segment companies often have difficulties in passing on higher raw material prices to OEMs. At the same time current problems in the automotive sector like Dieselgate and Worldwide harmonized Light vehicles Test Procedure (WLTP) could impact the profitability/liquidity of suppliers. We continue to be more cautious when underwriting small steel traders, especially those without additional business like prefabrication and weak equity ratios, as they often face strong competition and low margins.

We pay particular attention to recent financial information (balance sheets, interim figures, bank status, payment terms, duration of contract, order volume, payment behaviour). Due to the challenges mentioned above major strains cannot be ruled out for German steel and metals producers in the medium-term – with sales and profit decreases for many businesses along the value chain, coupled with a surge in payment defaults and business failures.

German steel/metals sector

Strengths	Broad range of customer industries and export destinations
	High quality/niche products
	High technology level compared to other competitors
Weaknesses	High energy costs
	Price pressure triggered by rising imports
	High dependency on raw materials
	Persistent overcapacities

Source: Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing

Source: Atradius

TABLE OF CONTENS
FULL REPORTS
MARKET PERFORMANCE AT A GLANCE
OVERVIEW CHART
INDUSTRY PERFORMANCE

Italy

- **Weaker performance in 2019 expected**
- **Increasing payment delays and insolvencies expected in 2019**
- **Payments take 115 days on average**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months				✔	
Development of insolvencies over the coming 6 months				✔	
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance			✔		
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector			✔		
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months		✔			
General demand situation (sales)			✔		

Source: Atradius

After several years of subdued performance, the Italian steel industry has rebounded since 2016, mainly due to increased demand from the automotive sector and EU anti-dumping import duties on Chinese steel. According to the World Steel Organisation, Italian steel production increased 2.9% in 2017, and 3.4% in the period January-August 2018.

The rebound of steel prices has had a positive impact on the cash flow of producers. However, the performance of distributors and service centres has been impacted by higher prices for steel and metals, due to larger working capital requirements, with a negative effect on their cash flows.

Steel prices have started to decrease again since September 2018, mainly due to increased imports from outside the EU. While the impact of US import tariffs on the Italian steel and metals industry is considered to be low (just 3% of Italian steel exports are shipped to the US), further decline of steel prices as a result of additional steel inflow in the EU could result in the amortisation of current inventory and decreasing margins for businesses.

While EU safeguard measures help to mitigate the pressure on steel and metals prices driven by imports, other factors are having an adverse effect on sector performance. Demand from automotive is expected to decrease in the coming months, while demand from construction remains sluggish. The expected increase in production of the major Ilva steel plant after the takeover from ArcelorMittal (it is estimated that the plant will add three million tons of steel to the domestic market supply) could put further pressure on prices. Due to all those factors we expect more pressure on Italian steel and metal businesses margins and cash flows in 2019 compared to 2017 and 2018.

Italy: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	1.6	1.1	0.9
Sector value added growth (%)	1.5	1.6	1.7

Average sector growth over the past 3 years (%)	0.2
Average sector growth over the past 5 years (%)	0.8
Degree of export orientation	average
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

As steel and metals are highly cyclical sectors closely linked to GDP growth, any economic policy shift of the new government that would dampen Italy´s economic expansion or business investment would subsequently affect the performance.

After the good performance seen in 2016 and 2017 payment delays and insolvencies have started to increase slightly in H2 of 2018. We expect this trend to continue in 2019. Businesses operating in the domestic market remain affected by slow payment from their customers, as the average payment duration is 115 days.

Italian steel/metals sector

Strengths	Flexible production
	Export oriented
	Consolidation in certain sectors
Weaknesses	Slowdown in demand both at domestic and European level
	Market remains quite fragmented
	High dependence on construction

Source: Atradius

Our underwriting stance is generally open to neutral, depending on the performance of the subsectors and their main buyer industries. We are more open to steel manufacturers and to export-oriented companies, while more attention is advised for businesses dependent on domestic construction and the oil and gas sector.

We also monitor players linked to automotive sector more closely due to the expected decrease in demand from this key buyer industry in 2019. We remain more cautious with the steel and metals distributors and service centre segment, which is characterised by a large number of relatively small companies that do not add a lot value, have thin margins, and are highly leveraged.

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

United Kingdom

- **Revenues have improved, but challenges remain**
- **Payments take 60 days on average**
- **No major insolvency increase expected in 2019**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance	✔				
Overall indebtedness of the sector	✔				
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months				✔	
General demand situation (sales)			✔		

Source: Atradius

In 2017 and H1 of 2018 the British steel and metals industry benefited from increased market prices which, despite a recent decrease, currently remain at an acceptable level. British steel and metals businesses have been generally able to increase their revenues, buoyed not only by higher prices, but also by increases in tonnage sold at acceptable margins. At the same time, Tata Steel´s merger with ThyssenKrupp has removed some of the uncertainty over a major decrease in domestic steel production in the short- to medium-term.

The impact of US import tariffs on British steel and aluminium exports is considered low. Most of those exports consist of highly engineered steel and metal items which currently are not produced in the US and not easily substitutable, meaning that tariff-related price increases can be passed on to buyers. Meanwhile, the EU has put safeguarding measures in place in order to protect the European market from excessive imports.

That said, those EU safeguarding measures could become a concern if the EU and the UK fail to reach a comprehensive agreement on the post Brexit EU-UK trade relationship or if there is a hard Brexit. Potentially, British steel and metals exports could become subject to the EU measures put in place to protect domestic steel. At the same time, with no preferential tariffs or simply no tariffs at all on non EU trade, the UK and its steel/metals industry could become vulnerable to cheap imports from Asia and the Middle East.

UK steel stockholders are mainly long established and profitable but also heavily reliant on bank finance (mainly invoice discounting) in order to have stock available as and when it is required. Usually they have low overheads, which makes them resilient to economic changes, as they are able to unwind inventories in order to free up cash. Banks are generally willing to provide loans to the industry. Historically service centres and steel stockhold-

United Kingdom: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	1.7	1.3	1.5
Sector value added growth (%)	5.9	3.5	1.9

Average sector growth over the past 3 years (%)	-2.6
Average sector growth over the past 5 years (%)	-4.9
Degree of export orientation	low
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

ers struggled to obtain decent margins against continuously depressed prices. However, the challenge now is to maintain strong margins when price volatility is endemic. Profit margins of many stockholders have come under pressure over the past 12 months due to rising prices, as the costs of replacing the stocks sold has risen faster than what has been termed as the outsell price, causing a lag in time before those prices can be passed on.

The average payment duration in the UK steel and metals industry is 60 to 90 days. It is expected that non-payment notifications will level off in the coming months. While UK business insolvencies are forecast to increase 8% in 2018 and 4% in 2019, it is expected that the steel and metals sector will not follow this deterioration trend.

British steel/metals sector

Strengths	Investment in new technologies
	Abundant access to external financing
Weaknesses	Volatile profit margins
	High dependence on the construction sector

Source: Atradius

For the time being our underwriting stance for all main steel and metals subsectors remains neutral. While financial analysis remains a key part of the decision making process understanding the strategic plans of businesses is just as important. A business starting to sell stock below market rates in an attempt to generate cash is a warning sign. Circumstances that could lead to such action might be prices decreasing below the purchase price or high stock costs being carried in a stagnating market.

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing

Source: Atradius

United States

- Import tariffs on steel and metal imports hurt certain segments
- Major buyer industries are about to be affected by higher prices
- A slight insolvency increase in 2019 cannot be ruled out

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months		✔			
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months		✔			
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector			✔		
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

According to the World Steel Association, US steel production increased 4% in 2017 and in the period January-August 2018 respectively. US steel demand is forecast to increase about 3% in 2018 and 2% in 2019, after a 6.4% increase in 2017. Last year US steel and metals businesses benefited from tax cuts on corporations, which allowed companies to expand their infrastructure and increase investments.

The imposition of import tariffs on steel and aluminium by Washington in spring 2018 has resulted in adjusted pricing in the US market. This has led to increasing revenues and improved profitability for US steel and metal producers, as domestically produced steel and metals is now less expensive than imported products.

That said, depending on the level of international sourcing, mid-level producers, smaller steel and metals service centres and end-buyer sectors have started to feel cash flow and profit margin pressure related to the working capital lag associated with the higher prices (especially for steel and aluminium). The new tariffs have made US steel and aluminium products a “first choice” of purchases, but at the same time many foreign producers offer specialized products not readily available in the US. Historically US-made steel and metals items have been produced at a higher cost compared to imports.

This means that many steel/metals trading or processing businesses in the US need to pay the additional tariff amount or higher prices for domestic products, but cannot pass the cost increase on to their costumers/end buyers in the short-term, because of existing contracts in place. Even after those contracts expire in 2019 the main issue for businesses importing steel and metal products will remain the ability to pass on increased costs to end buyers.

USA: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	2.2	2.9	2.5
Sector value added growth (%)	4.2	6.1	4.1

Average sector growth over the past 3 years (%)	-2.6
Average sector growth over the past 5 years (%)	-1.0
Degree of export orientation	medium
Degree of competition	medium

Sources: Macrobond, Oxford Economics, Atradius

The steel and aluminium tariff issue could potentially have an adverse impact on the US economy itself, especially on major steel/metals end-buyer sectors like automotive, construction and consumer durable goods (major kitchen appliances such as refrigerators and stoves/ovens). All those segments are highly dependent on steel and metal (especially aluminium) products, often sourced from abroad. Not passing on tariff-related price increases would affect businesses financials, while passing them on to end-consumers could reduce demand. For instance, it is expected that the automotive sector will reduce the production of new models due to lower consumer demand triggered by higher end-prices. In the construction industry, higher steel and metal prices could delay new projects. In order to meet budget targets financiers and builders could reduce the size of projects.

US steel/metals sector

Strengths	Businesses´ financial situation is generally stable
	Payment trends are currently stable and bank-supported financing is available for the time being
	Steel mills and recyclers show improved strength as tariffs on foreign product make their operations more profitable
Weaknesses	The inability of mid-level and small companies to absorb price increases due to tariffs could result in increased insolvencies in 2019
	The implementation of tariffs has caused foreign countries to reciprocate with tariffs on US products.
	Uneven pricing is beginning to affect smaller companies as costs cannot be readily passed on to end buyers.

Source: Atradius

The average payment duration in the US steel and metals sector remains, on average, 30-45 days domestically and 60-90 days for businesses abroad. Payment delays and defaults have decreased in 2017 due to the improved performance seen last year.

However, as the consequences of import tariff have begun to impact certain segments a slight increase in steel and metal insolvencies in the coming 12 months cannot be ruled out, especially as smaller players cannot afford to pay higher prices for tariff-related products.

Our underwriting stance for the steel and metals sector is generally neutral. While businesses like steel mills and recyclers are benefitting from the import tariffs, steel and metal traders, service centres and processors are struggling to digest higher costs, not being able to pass on the increase to end-customers for the time being.

Therefore, each buyer must be reviewed on a stand-alone basis. We seek a clear understanding of each buyer's domestic/international revenue split and the dynamics of their supply chain.

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

Market performance at a glance

Canada

- The sector is highly exposed to US import tariffs of 25% on steel and 10% on aluminium, as exports to the US amount to more than 80% of all Canadian steel and metals exports, affecting 45% of domestic steel production. In 2017, steel and aluminium shipments accounted for 3% of Canada's total merchandise exports to the US, and about 2% of the country's total exports.
- Currently the impact on the industry is difficult to determine as it is unclear whether the US tariffs will be long lasting for Canada. In any case, with the preliminary agreement of the new USMCA Agreement (replacing NAFTA) the outlook has improved that for Canada the tariffs will be removed in the foreseeable future.
- In H1 of 2018 results of many Canadian steel and metal businesses were still positive. Canadian exports benefited from a weaker exchange rate of the CAD against the USD. However, in H2 of 2018 and into 2019 it is expected that the US tariffs will affect performance. Competition in the market strongly intensified at the end of H1of 2018 as customers were shortening orders due to the uncertainty caused by the US tariffs. While it was originally expected to see more consolidation in the industry, this has not yet materialised, and with the improvement of the outlook we are not anticipating any change.
- Payments in the Canadian steel and metals sector take 65 days on average, and payment experience has been good over the past two years. It is expected that both payment delays and insolvencies will increase until the new USMCA trade agreement is ratified and the US import tariff issue is resolved.
- Our underwriting stance is generally neutral for the steel and metals industry, based on a more optimistic outlook after the USMCA agreement. We are cautious in our assessments should buyers be impacted by the US tariffs, but are supporting cover based on positive financial, bank and credit agency data.

Canada: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	3.0	2.1	1.7
Sector value added growth (%)	3.8	4.2	2.7

Average sector growth over the past 3 years (%)	0.1
Average sector growth over the past 5 years (%)	1.1
Degree of export orientation	average
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

China

- In the Chinese steel and metals industry overcapacity remains a major challenge, despite a combined 120 million ton reduction of total crude steel output in 2016 and 2017. Domestic steel and metal demand is expected to remain robust, supported by increased infrastructure spending. However, challenges have increased beyond further capacity reduction, due to the US steel and metals import tariffs and the ongoing trade dispute with Washington.
- While the amount of steel exports to the US is rather low (1.6% of total Chinese steel exports went to the US in 2017), the impact on Chinese aluminium producers and traders is much larger. However, facing deteriorating sales in the US many aluminium businesses have redirected exports to other regions (e.g. Europe, Southeast Asia) and enjoy government support (tax rebates). That said, longer lasting US import tariffs and/or an escalation of the trade conflict with the US would undoubtedly harm the industry.
- Despite some improvements over the last 12 months, the profit margin situation of many Chinese steel and metals businesses remains rather bad. Increased coking coal prices will have an adverse effect on the profit margins of steel producers if higher prices cannot be passed on accordingly. High leverage of businesses has been an outstanding issue over the last couple of years, and while most state-owned steel and metal companies still enjoy good bank facility support, private businesses face more troubles. However, it seems that even state-owned businesses cannot take government support for granted any more, especially in poor-performing steel and metals segments.
- As in 2017, payments in the Chinese steel and metals industry take between 60 and 120 days on average. The number and amount of protracted payments and insolvencies remains high. While leading state-owned steel makers still show some resilience, many private-owned steel and metals producers face serious troubles. The majority of private Chinese steel and metals traders do not have many fixed assets, and suffer from slim margins and very limited bank facilities.
- Given the poor credit risk situation in the industry, our underwriting stance remains very restrictive, with cover strictly limited to businesses with strong financial profiles or backgrounds.

China: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	6.9	6.6	6.0
Sector value added growth (%)	0.3	1.3	3.1

Average sector growth over the past 3 years (%)	1.5
Average sector growth over the past 5 years (%)	4.2
Degree of export orientation	average
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing

Source: Atradius

Czech Republic

- The domestic demand situation for steel and metals is currently good, driven by robust demand from automotive, engineering, and construction. Profit margins of steel and metal businesses improved in H1 of 2018 due to stable sales prices and a general price increase since 2016. Margins are expected to remain stable in the coming six months.
- Payments in the Czech steel and metals sector take 60-90 days on average. Payment experience has been good over the past two years, and both payment delays and insolvencies are expected to remain stable in the coming months. The insolvency level in this segment is low compared to other industries.
- Our underwriting stance is generally neutral for the iron and steel segment, as local steel production decreased 14% year-on-year in 2017 due to reconstruction and modernisation of domestic steel mills. At the same time the local steel sector is facing overcapacities and competition of cheaper producers from Asia. That said, our underwriting stance is open for the metals and metals manufacturing subsectors. Both segments currently benefit from a positive price development, stable margins, a good level of orders and good access to external financing.
- The main potential downside risk for the industry is a deterioriation in orders from main buyer industries, especially from the automotive sector. To a certain extent sales price volatility seems to be managable for steel and metals companies. The Czech steel and metals sectors are highly export-oriented with the EU as the main destination, while the US market accounts for just 3% of Czech steel and metals exports. Therefore, the impact of US import tariffs is rather low.

Czech Republic: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	4.5	3.0	2.7
Sector value added growth (%)	0.5	2.8	3.7

Average sector growth over the past 3 years (%)	-0.9
Average sector growth over the past 5 years (%)	-1.5
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

The Netherlands

- Although the steel and metals sector accounts for just 1.1% of Dutch GDP, it is important as a leading supplier for construction, automotive and machinery. The industry is highly dependent on domestic construction sector performance.
- After some difficult years, the industry has benefitted since late 2015 from a rebound in the domestic building sector, as well as rising demand from automotive and machinery and from increased exports. The overall outlook for 2019 remains positive. As the industry consists mainly of steel traders and wholesalers, the impact of the US import tariffs is very limited.
- However, due to overcapacity there is on-going price pressure in most segments, which negatively affects margins. However, due to the benign demand situation, profit margins are expected to remain stable in the coming 12 months. Innovation continues to be important in order to focus on efficiency and to reduce costs.
- Dutch steel makers, traders and wholesalers are higly dependent on banks for financing their stock. Banks have become more willing to lend than in previous years due to the economic rebound. However, any major steel price deterioration in the future would again make it harder to obtain additonal credit facilities.
- Payments in the Dutch steel and metals sector take 45 days on average. Payment delays and insolvencies are expected to remain stable in the coming months. The insolvency level in this segment is quite low.
- Our underwriting stance is generally open due to the current positive performance and outlook. We monitor stock levels more closely and low value added steel and metals companies, as they are very sensitive to price fluctuations. Also companies that are highly dependent on the oil and gas and shipbuilding sectors have our special attention due to lower order levels in the past..

The Netherlands: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	3.0	2.8	1.7
Sector value added growth (%)	1.8	0.8	1.4

Average sector growth over the past 3 years (%)	0.5
Average sector growth over the past 5 years (%)	1.8
Degree of export orientation	medium
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

Poland

- Domestic steel production is dominated by large global players like ArcelorMittal. Along the value chain between mills and final consumers of steel there are a lot of specialised manufacturers and distributors.
- The direct impact of US import tariffs is low given the limited share of exports to the US (5% of total Polish steel exports). However, pressure on prices and margins has increased due to higher steel imports into the EU in H1 of 2018.
- Profit margins of Polish steel and metal businesses are additionally impacted by fierce competition in the domestic market, especially in the steel and metals distribution segment. The costs of complying with high EU environmental standards put Polish producers at a disadvantage to non-EU producers. Another issue is the rising cost of electricity. While profit margins have improved over the last 12 months they are expected to level off or even decrease in 2019.
- Access to bank financing has further improved over the last 12 months, and banks are generally willing to provide loans to the industry. Payment experience has been good over the past two years, and steel and metals business insolvencies have been stable so far in 2018. However, it cannot be ruled out that both payment delays and insolvencies will increase in 2019, especially if price and margin pressures rise and/or should a slowdown in the construction industry, as the largest consumer of steel, materialises.
- Our current underwriting approach is positive to neutral due to the satisfactory performance seen in 2017 and H1 of 2018, a period in which businesses were able to accumulate capital and increase their financial resilience. However, due to new tax regulations regarding the reverse charge mechanism for construction businesses, we are observing increased concerns among steel and metals distributors dependent on the building industry.
- Last year a (still voluntary) split payment scheme aimed at reducing VAT fraud has raised concerns about deteriorating liquidity due to the freezing of businesses' funds related to VAT on a dedicated account. Thus far, this has had less impact on businesses liquidity than previously anticipated.

Poland : Iron and Steel

	2017	2018f	2019f
GDP growth (%)	4.6	4.6	3.2
Sector value added growth (%)	12.2	5.7	4.0

Average sector growth over the past 3 years (%)	4.1
Average sector growth over the past 5 years (%)	3.0
Degree of export orientation	medium
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing

Source: Atradius

Spain

- According to the World Steel Association, Spanish steel production increased 6.6% year-on-year in 2017, to 14.5 million tons, while exports increased 5.8%. Domestic steel consumption also increased last year (up 8%).
- Due to increasing sales prices and higher demand since H2 of 2017, especially from the construction sector, Spanish steel production rose again in 2018, by 3.3% year-on-year between January and July.
- Profit margins are expected to remain stable in the coming months. The direct impact of US import tariffs on the steel and metals sector is low given the limited share of exports (about 5% of total Spanish steel exports) to the US. While the risk of decreasing steel prices remains, due to surplus exports from outside the EU (especially from Russia and Turkey), it seems that additional safeguard measures set up by the EU will be a strong mitigating factor.
- The competitiveness of the domestic steel and metals industry remains negatively impacted by power costs, which are about 30%-50% higher than in France or Germany. This is of major importance for the sector, given that 75% of Spanish steel producers work with electric furnaces.
- Payment experience has been good over the past two years, and both payment delays and insolvencies remained stable in 2017 and H1 of 2018, and are expected not to increase in the coming months.
- However, our underwriting stance for the steel sector remains neutral to cautious due to the potential downside risks (escalation of trade disputes, eurozone growth deceleration, decreasing demand from major buyer industries like automotive and construction). We closely monitor businesses that are vulnerable to US import tariffs and price fluctuations..

Spain: Iron and Steel

	2017	2018f	2019f
GDP growth (%)	3.0	2.5	2.3
Sector value added growth (%)	5.1	3.2	1.9

Average sector growth over the past 3 years (%)	2.3
Average sector growth over the past 5 years (%)	2.0
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Iron and Steel	Metals	Metals Manufacturing
		

Source: Atradius

Industries performance forecast per country

November 2018

	Agriculture	Automotive/ Transport	Chemicals/ Pharma	Construction Const.Mtrls	Consumer Durables	Electronics/ ICT	Financial Services
Austria	⛅	🌧️	⛅	⛈️	☁️	☁️	☀️
Belgium	☁️	☁️	☀️	🌧️	☁️	⛅	☁️
Czech Rep.	⛅	☁️	⛅	🌧️	☁️	☁️	⛅
Denmark	⛈️	☁️	⛅	☁️	🌧️	☁️	☁️
France	🌧️	☁️	☀️	🌧️	☁️	☁️	⛅
Germany	☁️	☁️	☀️	☁️	☁️	☁️	⛅
Hungary	☁️	☁️	⛅	☁️	☁️	☁️	☁️
Ireland	☁️	☁️	⛅	⛅	☁️	⛅	⛅
Italy	⛅	⛅	⛅	🌧️	☁️	⛅	⛅
The Netherlands	⛅	☁️	☀️	⛅	☁️	⛅	⛅
Poland	☁️	🌧️	☁️	🌧️	🌧️	🌧️	⛅
Portugal	☁️	☁️	🌧️	🌧️	☁️	☁️	🌧️
Russia	🌧️	☁️	🌧️	🌧️	☁️	🌧️	☁️
Slovakia	☁️	⛅	⛅	🌧️	☁️	☁️	⛅
Spain	☁️	☁️	⛅	🌧️	☁️	☁️	☁️
Sweden	⛅	☁️	⛅	🌧️	⛅	⛅	⛅
Switzerland	⛅	☁️	⛅	🌧️	☁️	☁️	☀️
Turkey	⛅	⛅	☁️	⛈️	☁️	🌧️	⛅
UK	☁️	☁️	⛅	🌧️	☁️	☁️	☁️
Brazil	☁️	🌧️	☁️	🌧️	⛈️	⛈️	⛅
Canada	☀️	☁️	☁️	☁️	☁️	☁️	☀️
Mexico	☁️	⛅	☁️	🌧️	☁️	☁️	⛅
USA	☁️	☁️	⛅	☁️	☁️	⛅	⛅
Australia	⛅	🌧️	☁️	🌧️	☁️	⛅	⛅
China	☀️	☁️	☁️	🌧️	☁️	☁️	☀️
Hong Kong	☁️	☁️	☁️	☁️	☁️	⛅	⛅
India	☁️	☁️	⛅	🌧️	☁️	☁️	☁️
Indonesia	☁️	☁️	☁️	☁️	☁️	☁️	⛅
Japan	⛅	☁️	☁️	☁️	☁️	⛅	⛅
New Zealand	⛅	🌧️	⛅	⛅	🌧️	⛅	⛅
Singapore	⛅	🌧️	☁️	🌧️	☁️	☁️	⛅
Taiwan	☁️	🌧️	☁️	☁️	⛅	⛅	☁️
Thailand	☁️	⛅	☁️	☁️	☁️	☁️	⛅
United Arab Emirates	⛅	☁️	☁️	🌧️	🌧️	🌧️	⛅

	Food	Machines/ Engineering	Metals	Paper	Services	Steel	Textiles
	Good	Good	Fair	Fair	Good	Poor	Poor
	Good	Fair	Fair	Poor	Poor	Good	Poor
	Good	Good	Fair	Fair	Fair	Fair	Poor
	Good	Fair	Fair	Bleak	Fair	Poor	Poor
	Fair	Fair	Fair	Poor	Fair	Fair	Poor
	Fair	Good	Fair	Poor	Good	Fair	Poor
	Fair	Good	Poor	Fair	Good	Poor	Poor
	Good	Fair	Fair	Bleak	Fair	Fair	Poor
	Good	Excellent	Fair	Fair	Fair	Fair	Poor
	Excellent	Good	Good	Fair	Good	Fair	Fair
	Fair	Poor	Fair	Fair	Good	Fair	Fair
	Fair	Fair	Poor	Poor	Good	Poor	Poor
	Fair	Bleak	Fair	Fair	Poor	Fair	Fair
	Good	Good	Fair	Fair	Fair	Fair	Poor
	Good	Fair	Fair	Poor	Good	Fair	Poor
	Good	Good	Poor	Fair	Fair	Poor	Poor
	Good	Good	Fair	Fair	Good	Poor	Fair
	Good	Fair	Bleak	Poor	Poor	Fair	Poor
	Fair	Fair	Fair	Poor	Fair	Fair	Poor
	Good	Poor	Poor	Fair	Fair	Poor	Poor
	Good	Fair	Fair	Poor	Good	Fair	Bleak
	Good	Fair	Poor	Good	Good	Poor	Poor
	Good	Fair	Fair	Poor	Good	Fair	Fair
	Good	Fair	Poor	Poor	Fair	Poor	Poor
	Good	Fair	Bleak	Poor	Good	Bleak	Poor
	Excellent	Fair	Poor	Fair	Good	Poor	Fair
	Good	Fair	Poor	Good	Good	Poor	Fair
	Good	Fair	Poor	Fair	Fair	Poor	Fair
	Good	Fair	Fair	Fair	Good	Fair	Poor
	Fair	Fair	Fair	Poor	Poor	Poor	Poor
	Good	Fair	Fair	Fair	Good	Poor	Fair
	Excellent	Fair	Poor	Fair	Good	Poor	Fair
	Good	Fair	Fair	Fair	Fair	Poor	Bleak
	Poor	Fair	Poor	Fair	Good	Poor	Poor

Excellent

Good

Fair

Poor

Bleak

Industry performance

Changes since October 2018

The Americas

Canada

Metals

Up from Bleak to Fair

Steel

Up from Bleak to Fair

See article on page 15.

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